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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1940

No. 737

JEAN LOUISE MATTHEWS, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED JANUARY 31, 1941.

CERTIORARI GRANTED MARCH 10, 1941.

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Docket Entries

1

DOCKET NO. 96237

MRS. JEAN LOUISE MATTHEWS,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Appearances:

2

For Petitioner: Joseph C. White, Esq., Richard H. Wilmer, esq.

For Respondent: John R. Wheeler, Esq.

DOCKET ENTRIES:

1938

Nov. 23—Petition received and filed. Taxpayer notified. (Fee paid.)

Nov. 23—Copy of petition served on General Counsel.

1939

3

Jan. 17—Answer filed by General Counsel.

Jan. 17—Request for Circuit hearing in New York City filed by General Counsel.

Jan. 20—Notice issued placing proceeding on New York City Calendar. Copy of answer and request served.

Sept. 19—Hearing set Nov. 13, 1939, New York, N. Y.

Nov. 14—Hearing had before Mr. Murdock, on the merits. Submitted. Consolidated with 96066, 96235-36. Stipulation of facts filed. Briefs due in 60 days —replies due in 15 days.

4 *Docket Entries*

1940

Jan. 12—Motion for extension to Jan. 28, 1940 to file brief filed by General Counsel.

Jan. 16—Notice of appearance of Richard H. Wilmer as counsel filed.

Jan. 16—Motion for leave to file attached printed brief filed by taxpayer. 1/18/40 granted.

Jan. 18—Brief filed by taxpayer.

Jan. 23—Motion for leave to file brief filed by General Counsel—brief lodged. 1/24/40 granted.

5

Jan. 24—Copy of brief served on General Counsel.

Feb. 1—Memorandum reply brief filed by General Counsel.

Feb. 6—Reply brief filed by taxpayer. 2/6/40 copy served.

May 31—Memorandum opinion rendered—Mr. Murdock, Division 3. Decision will be entered for respondent.

May 31—Decision entered—J. E. Murdock, Division 3.

Aug. 27—Petition for review by U. S. Circuit Court of Appeals, Second Circuit, with assignments of error filed by taxpayer.

6

Aug. 27—Proof of service filed by taxpayer.

Aug. 27—Praecipe filed by taxpayer.

Aug. 27—Proof of service filed by taxpayer.

Petition

UNITED STATES BOARD OF TAX APPEALS

Docket No. 96237

MRS. JEAN LOUISE MATTHEWS,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:A:1-JMF:90D) dated August 25, 1938, and as a basis of her proceeding alleges as follows:

1. The petitioner is an individual with residence at 2801 Pine Tree Drive, Miami Beach, Florida. The return for the period here involved was filed with the Collector for the Fourteenth District of New York.

2. The notice of deficiency (copy of which is attached and marked Exhibit A) was mailed to the petitioner on August 25, 1938. Also attached hereto and marked Exhibit B is Schedule I-A of the report of examination dated March 29, 1938, referred to in the statement attached to said notice of deficiency.

3. The taxes in controversy are income taxes for the calendar year 1934 and in the amount of $9,604.99.

4. The determination of tax set forth in said notice of deficiency is based upon the following error:

10 *Petition*

(1) Substitution of the basis of $68,630.89 in lieu of a basis of $122,943.62 in the computation of a profit on the sale of the 1,919 shares of the preferred stock of Standard Oil Export Corporation.

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) On May 20, 1913, one Henry M. Flagler, a resident of St. Johns County, Florida, died testate leaving a last will and testament dated February 1, 1902 and seven codicils
11 dated respectively February 17, 1903; April 28, 1904; January 8, 1906; April 7, 1908; December 22, 1910; January 10, 1912; and September 13, 1912; which said last will and testament and codicils thereto were duly admitted to probate in Court of County Judge in and for St. Johns County, Florida, on May 24, 1913.

(b) Item Third of said last will and testament provided as follows:

"I have been for many years investing in railroads, hotel and land companies in the state of Florida, and it is my intention in the future to foster, protect and
12 properly develop such properties, and to provide against my decease while such properties are in the processes of development and to relieve my beloved wife, hereinafter named, from the immediate cares and responsibilities of so varied and such extensive interests, I hereby declare a trust concerning all my property, both real and personal, and wheresoever situated, except what is covered by the 'Fourth' Item of this instrument, and may be necessary for the expense of administration by my executors, including court costs, to my Trustees above named, which trust shall be and continue for the length of time hereinafter by this instrument provided."

(c) Said last will and testament after providing in Item Fourth for certain relatively small bequests provided in Item Fifth thereof as follows:

> "The balance of my estate I place, according to the purpose declared in the 'Third' Item of this instrument, in the hands of my said Trustees to be used, managed and controlled by them and their successors for the purpose of protecting, fostering, operating and developing during the life of such trust, all my Florida Properties according to the purposes indicated by the charters of the several companies, and as nearly along the lines which I have adopted, or may hereafter adopt, as may be consistent with their judgment, and discretion under the conditions which may hereafter exist. The said trust shall continue for five years from the time of my death, and if at the end of such five years the condition of the Florida East Coast Railway Company and the Florida East Coast Hotel Company (they being my Florida Railroad and hotel properties referred to) or of either of them should be such as to require financial aid from sources outside of themselves or itself, then I direct that such trust shall continue so long as either or both of such last named companies shall require such assistance, but not longer, however, than a period of five years from the termination of the above mentioned or first period of five years. It is, however, to be distinctly understood that I do not authorize the railroad of said Railway Company extended south of Miami and no power to do so is given hereby."

(d) Item Sixth of said last will and testament provided in part as follows:

> "During the existence of said trust I charge said trust estate with the payment of the following annuities and expenses and direct that the same be paid by the Trustees:
>
> "1. To my dearly beloved wife, Mary Lilly Flagler, the annual sum of One Hundred Thousand Dollars

16 *Petition*

($100,000) payable in quarterly installments from the date of my decease; and I further direct that so much of the annual net income from said trust property over and above the said annuity and that hereinafter by subsequent clause of this item provided for, as shall not be required during the extended or second period of said trust, provided for in the 'Fifth' Item of this instrument shall be paid to my said wife annually."

(e) Item Seventh of said last will and testament provided in part as follows:

17 "in the event that at the expiration of said trust there shall be any child or children of my said son living, then I direct that eight thousand shares of the stock of the said Standard Oil Company shall be delivered, assigned and transferred to such child or children as shall then be living, such children, if there be more than one child, to take such stock in equal proportions, and should there be no child of my said son living at the termination of said trust, then such eight thousand shares of stock shall remain a part of such trust estate and go to my wife with the balance of the residue thereof the same as if no provision had been made herein as to such eight thousand shares of stock."

18 (f) The petitioner herein is one of the children referred to in the foregoing quotation from Item Seventh of said last will and testament and was born prior to May 20, 1913.

(g) Item Ninth of said last will and testament provided as follows:

"All the rest, residue, and remainder of my estate whether real or personal and wheresoever situate, including of course all property covered by or included in said trust and not payable out of the same or at the end of said trust and all other property and estate of any and every kind whatsoever, I give, devise

and bequeath to my beloved wife, Mary Lily Flagler (formerly Mary Lily Kenan of Wilmington, North Carolina) forever, and I hereby authorize, empower, and direct my said executors and Trustees to pay over and transfer to my said wife at the expiration of said trust all such estate and property. And it is my intention to include in this gift, bequest and devise all accumulations or enlargements of my estate and property as shall have arisen during the life and operation of said trust; and it is also my intention to include in such devise my summer home at Mamaroneck, in the County of Westchester, state of New York, and my property, Number Twenty-one West Fifty-fifth Street in the City of New York, state and county of New York."

(h) Item Tenth of said last will and testament provided in part as follows:

"For the purpose of the fulfillment and due execution of the above trust I hereby invest my Trustees with full power and authority to execute all such instruments, obligations, assignments or transfers as may be necessary in the course of their business as such Trustees and to renew, refund, and by new obligation to provide for the extension, adjustment and payment of any and all obligations that I may leave outstanding at the time of my decease, to the end that if possible all and any such obligations shall be paid and discharged out of the income of my estate during the continuance of such trust.

* * * * * * * *

"It is my will and intention, in so far as I am legally able to do so to exempt my Trustees in the matter of investment and reinvestment of any portion of my estate from the limitations as to the classes of securities that may be named in the provisions of the statutes of the state of Florida or of any other state or of the United States in respect to the investment of the proceeds and income of trust estate; the principal object of this exemption being that if any of the

various enterprises, companies or corporations referred to above in which I am interested shall require temporary assistance the provisions of such statutes shall not interfere to prevent any loan to or on account of such companies or corporations as in the absence of such statutory restrictions might seem wise or advisable on the part of my said Trustees; it is, however, not my intention that any such assistance shall be extended to any other than the following companies:

"The Florida East Coast Railway Company, and the Florida East Coast Hotel Company."

(i) Item Third of the codicil of said Henry M. Flagler dated January 8, 1906, provided in part as follows:

"I wish to, and do hereby amend the 'Tenth' Item of my said original will by adding at the end of the first paragraph thereof the following, to wit:

"In view of the Florida East Coast Railway Company having determined to extend and being now engaged in extending its railway to the City of Key West, I hereby authorize said trustees to borrow from time to time money in such sums and upon such terms as they may find necessary and deem proper to enable said Florida East Coast Railway Company to make such extension including also the purchase and construction of terminal facilities and rolling stock and other equipment, and every proper purpose incidental to such enterprise, and to pledge so much of the trust properties as may be necessary for the payment of such loans, and to lend on such terms as they may deem proper, such money to said Florida East Coast Railway Company to be used by it for such purposes."

(j) Item First of the Codicil of said Henry M. Flagler, dated September 13, 1912, provided as follows:

"Whereas in my said last will and testament, I have bequeathed to my son, and to his children, in the manner described and provided for in my said

last will and testament, certain shares of Standard Oil stocks, therein more particularly designated and described, and whereas since the time of the making, publishing and declaring of my said last will and testament, certain changes in the form of said shares and the rights thereunder have taken place, by reason of which some uncertainty might arise as to my intentions in relation to the said bequests.

"Now to obviate any uncertainty relating thereto, I do hereby declare it to have been, and still to be my intention to include by the terms of shares of Standard Oil stocks, in my said last will and testament the said shares, or such other shares of stock, property and rights as have been, or may hereafter be issued to or received in the place and stead of said shares of Standard Oil stocks as the same existed at the time of the making of my last will and testament, excepting therefrom, however, such subscription rights under said stock or arising from the ownership thereof, as I have heretofore or may hereafter exercise and pay for."

(k) Pursuant to the provisions of Item Fifth of said last will and testament said trustees elected to continue said trust beyond the end of five years from the time of the death of said Henry M. Flagler and said trust did continue for a period of ten years from the time of the death of said Henry M. Flagler and terminated on May 20, 1923.

(l) Said trustees delivered, assigned and transferred to the petitioner subsequent to May 20, 1923, but as of that date, 8,000 ordinary shares of the stock of Anglo-American Oil Company, Limited. In 1925 the petitioner received a stock dividend of 2,666 ordinary shares of the stock of Anglo-American Oil Company, Limited in respect of said 8,000 shares of said stock, giving her an aggregate of 10,666 shares of said stock. On January 31, 1930, said 10,666 shares were exchanged for 1,919.88 shares of the preferred stock of Standard Oil Export Corporation. In 1930 the petitioner

28 *Petition*

sold the 88/100 share and in her income tax return for that year ascribed a tax basis thereto of $56.38.

(m) By a trust agreement dated July 2, 1931, the petitioner granted, assigned, set over, and delivered to Harry Harkness Flagler as trustee in trust certain securities including the 1,919 shares of the preferred stock of Standard Oil Export Corporation hereinbefore referred to.

(n) The fair market value of said 8,000 ordinary shares of the stock of Anglo-American Oil Company, Limited, on
29 May 20, 1923, was $123,000. The fair market value of said 1,919.88 shares of the preferred stock of Standard Oil Export Corporation on January 31, 1930, was $186,228.36.

(o) The tax basis of said 1,919 shares of preferred stock of Standard Oil Export Corporation in December, 1934, was not less than $122,943.62.

(p) In December, 1934, said Harry Harkness Flagler as trustee sold said 1,919 shares of the preferred stock of Standard Oil Export Corporation for which he received as such trustee the net amount of $212,110.60.

30 WHEREFORE, the petitioner prays that this Board may hear the proceeding, redetermine the deficiency alleged in said notice of deficiency, determine that the petitioner has made an overpayment of tax in respect of the taxable year herein involved, and grant such other and further relief as the Board shall deem proper.

Joseph C. White
JOSEPH C. WHITE,
15 Broad Street,
New York, N. Y.
Counsel for Petitioner

Petition

STATE OF NEW YORK, }
COUNTY OF NEW YORK, } ss.:

JEAN LOUISE MATTHEWS being duly sworn deposes and says:

That she is the petitioner above named; that she has read the foregoing petition or had the same read to her and is familiar with the statements contained therein; and that the statements contained therein are true except those stated to be on information and belief and that those she believes to be true.

JEAN LOUISE MATTHEWS.

Subscribed and sworn to before me
this 21st day of November, 1938.

ALFRED SHELDRICK
Notary Public, Kings County
Kings Co. Clerk's No. 436, Reg. No. 577
N. Y. Co. Clerk's No. 1134, Reg. No. O 8734
Bronx Co. Clerk's No. 49, Reg. No. 242 S40
Queens Co. Clerk's No. 571, Reg. No. 2571
Certificates filed also in
Richmond and Westchester Counties
Commission expires March 30, 1940

[NOTARIAL SEAL]

34 EXHIBIT A

Letterhead of
TREASURY DEPARTMENT

August 25, 1938

Mrs. Jean Louise Matthews,
32 Park Avenue,
New York, New York.

Madam:

You are advised that the determination of your income tax liability for the taxable year(s) ended December 31, 1934, discloses a deficiency of $9,604.99 as shown in the statement attached.

35

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency mentioned.

Within ninety days (not counting Sunday or a legal holiday in the District of Columbia as the ninetieth day) from the date of the mailing of this letter, you may file a petition with the United States Board of Tax Appeals for a redetermination of the deficiency.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C1:P-7. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency, and will prevent the accumulation of interest, since the interest period terminates thirty days after filing the form, or on the date assessment is made, whichever is earlier.

36

Respectfully,

GUY T. HELVERING,
Commissioner,
By W. T. SHERWOOD,
Acting Deputy Commissioner.

Enclosures:
Statement
Form of waiver

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STATEMENT

IT:A:1
JMF:90D

MRS. JEAN LOUISE MATTHEWS,
32 Park Avenue,
New York, New York.

TAX LIABILITY FOR TAXABLE YEAR ENDED DECEMBER 31, 1934

	Liability	Assessed	Deficiency
Income Tax.....	$144,807.28	$135,202.29	$9,604.99

38

In making this determination of your income tax liability careful consideration has been given to the report of examination dated March 29, 1938; to your protest dated March 2, 1938 and to the statements made at the conference held on June 24, 1938.

ADJUSTMENTS TO NET INCOME

Net income as disclosed by return.....	$274,037.32
Unallowable deductions and additional income:	
(a) Fiduciary	27,915.08
(b) Capital gain	16,293.82
Net income adjusted	$318,246.22

39

EXPLANATION OF ADJUSTMENTS

(a) This adjustment was made in a previous examination to which you consented in a signed agreement and the resulting deficiency in tax has been assessed.

280 U. S. 327 (1930). The analogous section in the Revenue Acts of 1928 and 1932 was somewhat different. In other words, Congress, in the Revenue Act of 1934, went back to the language used in the Acts prior to that of 1928 and reenacted that language.

In 1920 the Bureau of Internal Revenue issued a ruling under the Revenue Act of 1918 to the effect that where a remainderman has only a contingent interest in property prior to the death of the life tenant, the remainderman acquires the property only upon the death of the life tenant. O. D. 727, 3 C. B. 53. Twelve years later, in 1932, the General Counsel for the Bureau of Internal Revenue reaffirmed the position in G. C. M. 10260, XI-1 C. B. 79, saying at p. 80:

> "the position of this office has been that one who has a mere contingent interest does not 'acquire' the property in question until his interest becomes vested."

In at least three cases decided before the enactment of the Revenue Act of 1934 the courts had uniformly reached the same conclusion. *Pringle* v. *Commissioner,* 64 F. (2d) 863 (C. C. A. 9th, 1933), *cert. den.,* 290 U. S. 656 (1933), decided under the Revenue Act of 1921; *Lane* v. *Corwin,* 63 F. (2d) 767 (C. C. A. 2d, 1933), *cert. den.,* 290 U. S. 644 (1933), decided under the Revenue Act of 1928; *Anchor Realty & Investment Co.* v. *Becker,* 3 F. Supp. 22 (E. D. Mo., 1933), aff'd, 71 F. (2d) 355 (C. C. A. 8th, 1934), decided under the Revenue Act of 1928. Although there have been numerous cases decided after the enactment of the Revenue Act of 1934 your Petitioners have found no decision holding contrary to the above except

those of the Second Circuit in the *Van Vranken* and the instant cases.

In three cases decided by this Court on December 9, 1940, involving the identical problem of statutory construction it was held that the Commissioner's regulations attempting to change the well established meaning of statutory language that had been defined only by administrative rulings were invalid for the reason that the changes could be made only by Congress. *Helvering* v. *Janney, Taft* v. *Helvering,* and *Helvering* v. *Oregon Mutual Life Insurance Co.* (61 S. Ct. 241, 244 and 207).

For instance, in *Helvering* v. *Janney,* in holding the regulations invalid this Court said:

> "It was not until 1935 that the Treasury Department by Article 117-5 of Regulations 86 undertook to provide that 'the allowance of losses of one spouse from sales or exchanges of capital assets is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets'.
>
> "We are of the opinion that under the provision of the Act of 1934 as to joint returns of husband and wife, which embodied a policy set forth in substantially the same terms for many years, Congress intended to provide for a tax on the aggregate net income and that the losses of one spouse might be deducted from the gains of the other; and that this applied as well to deductions for capital losses as to other deductions. This, we think, was the meaning of the provision of the Revenue Act of 1934 when it was enacted, and it was subject to change only by Congress, and not by the Department."

In *Taft* v. *Helvering* this Court concluded as follows:

> "In 1935, by Article 23(o)-1 of Treasury Regulations 86, the Department sought to require a husband and wife, whether they make 'a joint return or separate returns', to base their deduction for charitable contributions on the separate net income of the spouse making them. We are of the opinion that under the Revenue Act of 1934, taken with the meaning we think it had when enacted, petitioners were entitled to the combined deductions they claimed, and that the departmental regulation to the contrary was ineffective to deprive them of that right."

Finally, in *Helvering* v. *Oregon Mutual Life Insurance Co.*, this Court said:

> "We find it unnecessary to discuss the extent to which such a regulation might, under different circumstances, be given retroactive effect by virtue of the statutory power of the Commissioner. Nor do we find it necessary to discuss the argument that the policy behind the special treatment afforded life insurance companies does not warrant allowing this deduction. For it is our conclusion that by section 203(a)(2) of the 1932 and 1934 Acts, Congress has granted life insurance companies a deduction for disability reserves which only Congress can take away."

The Commissioner's regulations involved in the instant cases are therefore invalid if the intention of Congress was, as the *Reynolds* case holds, to adopt the uniform administrative and judicial construction of § 113(a)(5) upon the reenactment of that Section in the Revenue Act of 1934. Under the most recent rulings of this Court it is for

Congress, and Congress alone, to change the meaning thus given the statutory language when originally enacted.

We, therefore, respectfully urge that this Court allow the writ.

Respectfully submitted,

ROSWELL L. GILPATRIC,
JOSEPH C. WHITE,
Attorneys for Petitioners.

MAURICE T. MOORE,
H. BRICE GRAVES,
Of Counsel.